

CHILDREN'S HOSPITAL
Audits of Consolidated Financial Statements
December 31, 2009 and 2008

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Release Date 7/14/10

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Independent Auditor's Report

To Children's Hospital
New Orleans, Louisiana

We have audited the accompanying consolidated balance sheets of Children's Hospital (the Hospital) as of December 31, 2009 and 2008, and the related consolidated statements of operations, changes in net assets, and cash flows for the years then ended. These financial statements are the responsibility of the Hospital's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of the Hospital as of December 31, 2009 and 2008, and the results of its operations, changes in its net assets, and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

A Professional Accounting Corporation

April 26, 2010

CHILDREN'S HOSPITAL
Consolidated Balance Sheets
December 31, 2009 and 2008 (In Thousands)

	2009	2008
Assets		
Current Assets		
Cash and Cash Equivalents	\$ 9,573	\$ 8,787
Patient Receivables, Net of Allowances for Uncollectible Accounts of \$4,143 and \$4,347 in 2009 and 2008, Respectively	24,720	22,482
Prepaid Expenses and Other Assets	12,406	12,421
Estimated Third-Party Payor Settlements	1,014	11,706
Due from LCMC	206	-
Total Current Assets	47,919	55,396
Assets Whose Use is Limited or Restricted		
By Board for Capital Improvements	505,323	491,685
By Board for Capital at Touro	96,879	-
By Donors	4,245	4,774
Total Assets Whose Use is Limited or Restricted	606,447	496,459
Property, Plant, and Equipment		
Land and Improvements	18,534	18,457
Buildings	100,624	94,388
Equipment	129,951	123,048
	249,109	235,893
Less: Accumulated Depreciation	(145,183)	(137,984)
	103,926	97,909
Construction in Progress	2,897	11,088
Total Property, Plant, and Equipment	106,823	108,997
Total Assets	\$ 761,187	\$ 660,853
Liabilities and Net Assets		
Current Liabilities		
Accounts Payable	\$ 14,015	\$ 16,390
Accrued Compensation	11,030	9,634
Other Current Liabilities	899	1,062
Total Current Liabilities	25,944	27,086
Net Assets		
Unrestricted	730,997	628,993
Temporarily Restricted	4,060	4,588
Permanently Restricted	186	186
Total Net Assets	735,243	633,767
Total Liabilities and Net Assets	\$ 761,187	\$ 660,853

The accompanying notes are an integral part of these consolidated financial statements.

CHILDREN'S HOSPITAL
Consolidated Statements of Operations
For the Years Ended December 31, 2009 and 2008 (In Thousands)

	2009	2008
Unrestricted Revenues, Gains and Other Support		
Net Patient Service Revenues	\$ 213,082	\$ 203,148
Contributions, Grants, and Other	12,811	11,994
Total Revenues, Gains and Other Support	225,893	215,142
Expenses		
Employee Compensation and Benefits	111,013	105,477
Professional Fees	23,763	20,298
Supplies and Other Expenses	46,550	43,429
Purchased Services	17,044	17,456
Provision for Bad Debts	4,750	4,297
Depreciation and Amortization	10,853	9,982
Total Expenses	213,973	200,939
Operating Income Before Investment Income (Loss), Other Non-Operating Loss and Community Support	11,920	14,203
Investment Income (Loss)	107,542	(233,453)
Other Non-Operating Loss	(4,521)	-
Community Support, Net	(12,937)	(12,795)
Increase (Decrease) in Unrestricted Net Assets	\$ 102,004	\$ (232,045)

The accompanying notes are an integral part of these consolidated financial statements.

CHILDREN'S HOSPITAL**Consolidated Statements of Changes in Net Assets****For the Years Ended December 31, 2009 and 2008 (In Thousands)**

	2009	2008
Increase (Decrease) in Unrestricted Net Assets	\$ 102,004	\$ (232,045)
Temporarily Restricted Net Assets		
Contributions and Grants	6,727	7,870
Net Assets Released from Restrictions	(7,255)	(9,325)
Decrease in Temporarily Restricted Net Assets	(528)	(1,455)
Increase (Decrease) in Net Assets	101,476	(233,500)
Net Assets, Beginning of Year	633,767	867,267
Net Assets, End of Year	\$ 735,243	\$ 633,767

The accompanying notes are an integral part of these consolidated financial statements.

CHILDREN'S HOSPITAL**Consolidated Statements of Cash Flows****For the Years Ended December 31, 2009 and 2008 (In Thousands)**

	2009	2008
Cash Flows from Operating Activities		
Increase (Decrease) in Net Assets	\$ 101,476	\$ (233,500)
Adjustments to Reconcile Increase (Decrease) in Net Assets to Net Cash Provided by Operating Activities		
Depreciation and Amortization	12,613	11,955
Provision for Bad Debts	4,750	4,297
Unrealized (Gain) Loss on Investments	(143,318)	253,411
Net Loss on Disposal of Assets	119	191
Changes in Assets and Liabilities		
Patient Receivables, Net of Allowances	(6,988)	(4,824)
Prepaid Expenses and Other Assets	15	(416)
Accounts Payable, Accrued Compensation, and Other Liabilities	(1,141)	(689)
Estimated Third-Party Payor Settlements	10,692	(10,015)
Assets Whose Use is Limited or Restricted, Net Due from LCMC	33,331	(9,779)
	(206)	-
Net Cash Provided by Operating Activities	11,343	10,631
Cash Flows from Investing Activities		
Purchases of Property, Plant, and Equipment	(10,557)	(16,977)
Increase (Decrease) in Cash and Cash Equivalents	786	(6,346)
Cash and Cash Equivalents, Beginning of Year	8,787	15,133
Cash and Cash Equivalents, End of Year	\$ 9,573	\$ 8,787

The accompanying notes are an integral part of these consolidated financial statements.

CHILDREN'S HOSPITAL

Notes to Consolidated Financial Statements

Note 1. Accounting Policies

Organization

The consolidated financial statements include Children's Hospital, Children's Hospital Medical Practice Corporation (CHMPC), and Children's Hospital Anesthesia Corporation, collectively, "the Hospital". CHMPC and Children's Hospital Anesthesia Corporation are wholly owned subsidiaries exempt from federal income taxes. All material intercompany accounts and transactions have been eliminated upon consolidation.

Children's Hospital and its subsidiaries are organized as non-stock, not-for-profit Louisiana corporations and are exempt from income taxes under Internal Revenue Code 501(c)(3). All corporate powers are vested in the Board of Trustees of Louisiana Children's Medical Center, the Hospital's non-profit parent.

The Hospital, located in New Orleans, Louisiana, is a 247-bed medical center that serves the entire Gulf South region, caring for infants, children, and adolescents from birth to 21 years of age. The Hospital provides inpatient services in all pediatric, medical, surgical, and psychiatric subspecialties with a staff of more than 400 physicians. Outpatient services are provided in more than 50 subspecialties. The Hospital also provides a large array of community benefit programs, wellness programs, research activities, and special programs for the handicapped and medically underserved.

CHMPC was incorporated on February 8, 1996, to manage pediatric physician practices in a high-quality, cost-effective manner. A division of CHMPC, Kids First, emphasizes providing pediatric care in medically underserved geographical areas. Children's Hospital Anesthesia Corporation was incorporated on June 30, 2000, to provide high-quality, hospital, comprehensive anesthesia services.

Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes and disclosure of contingent assets and liabilities. Actual results inevitably will differ from those estimates, and such differences may be material to the financial statements.

Cash and Cash Equivalents

Cash and cash equivalents include short-term, highly liquid investments, such as money market accounts and certain repurchase agreements with original maturities of three months or less.

CHILDREN'S HOSPITAL

Notes to Consolidated Financial Statements

Note 1. Accounting Policies (Continued)

Cash and Cash Equivalents (Continued)

Interest rate futures and options contracts are used by the Hospital on a limited basis to offset changes in market interest rates on its investment portfolio. If the options expire, the net premium paid or received is recorded as investment expense or income, respectively. If the options are exercised with the result that an investment instrument is bought or sold, the net premium paid or received attaches to the cost of that instrument.

Contributions and Donor - Restricted Gifts

The Hospital records contributions receivable in accordance with Financial Accounting Standards, Board Accounting Standards Codification (ASC) Topic, *Accounting for Contributions Received and Contributions Made*, which requires the organization to distinguish between contributions received for each net asset category in accordance with donor-imposed restrictions. Conditional promises to give and indications of intentions to give are reported at fair value at the date the condition is met or the gift is received. The gifts are reported as either temporarily or permanently restricted support if they are received with donor stipulations that limit the use of the donated assets. When an externally-imposed restriction expires or unrestricted contributions are realized, temporarily restricted net assets are reclassified to unrestricted net assets and reported in the statement of operations as net assets released from restrictions. Temporarily restricted gifts greater than \$100,000 used to purchase a depreciable asset are reclassified as unrestricted net assets over the same period of time that the related asset is being depreciated. Contributions for which the restrictions are met in the same period in which the unconditional promise to give is received are recorded as unrestricted revenue in the accompanying consolidated financial statements.

Contributions receivable are recorded at the present value of expected future cash flows discounted at 3.32%. Contributions are expected to be realized in the following periods (in thousands):

	2009	2008
In One Year or Less	\$ 76	\$ 56
Between One Year and Five Years	120	160
	<u>196</u>	<u>216</u>
Less Discount	(53)	(53)
Total	\$ 143	\$ 163

Management considers substantially all contributions to be collectible and, therefore, no allowance for uncollectible contributions is included in the table above. Contributions receivable are included in prepaid assets and other receivables on the consolidated balance sheets.

CHILDREN'S HOSPITAL

Notes to Consolidated Financial Statements

Note 1. Accounting Policies (Continued)

Assets Whose Use is Limited or Restricted

Assets whose use is limited primarily include assets set aside by the Board of Trustees for future capital improvements and commitments, over which the Board retains control and may, at its discretion, subsequently use for other purposes. In addition, there are assets donated to the Hospital that are restricted as to use by the donor.

LCMC's Health Care System Agreement, dated July 13, 2009, established a capital commitment in which Children's Hospital committed to provide funding of a minimum of \$100 million to its affiliate, Touro Infirmary, Inc. (Touro), over the next five years. The purpose of this funding is for the acquisition of capital items to benefit Touro. This \$100 million commitment is contingent upon the cash flows generated by Touro over this time period. These committed funds are reflected on the consolidated balance sheet as assets whose use is restricted by board for capital at Touro. Due to the contingency placed on this commitment, the expense and related reduction of this restricted asset will not be recorded by the Hospital until the funds are actually disbursed to Touro (see Note 14).

Assets whose use is limited consist primarily of mutual funds, debt securities and marketable equity securities, interest rate futures, options contracts, and money market accounts. These securities are classified as trading and are stated at fair value, based on quoted market prices. Gains and losses, both realized and unrealized, are included in net investment income in the consolidated statements of operations (see Note 2).

Net Patient Service Revenues and Related Receivables

Net patient service revenues and receivables are reported at the estimated net realizable amounts from patients, third-party payors, and others for services rendered, including estimated retroactive adjustments under reimbursement agreements with third-party payors. The Hospital provides care to patients even if they lack adequate insurance coverage or are covered by contractual payment arrangements that do not pay full charges. The payment agreements with certain commercial insurance carriers, health maintenance organizations, and preferred provider organizations are based on per diem rates or discounts from established charges.

Charity Care

The Hospital renders a significant amount of care to patients from whom no collections are expected. This program, the Children's Healthcare Assistance Plan ("CHAP") is reported as Community Support (see Note 8). The CHAP service revenue, write-offs and associated costs are not included in the Hospital operating income.

CHILDREN'S HOSPITAL

Notes to Consolidated Financial Statements

Note 1. Accounting Policies (Continued)

Statements of Operations

Operating income (loss) before investment income and community support includes hospital activity and excludes investment income and the Hospital's community support activities (see Notes 2 and 8).

The consolidated statements of operations include excess of revenues over expenses which is an indicator of financial performance. Changes in restricted net assets are excluded from excess of revenues over expenses, and include permanent transfers of assets to and from affiliates for other than goods and services, and contributions of long lived assets (including assets acquired using contributions by which donor restriction were to be used for the purposes of acquiring such assets).

Property, Plant, and Equipment

The Hospital records all property, plant, and equipment acquisitions at cost, except for assets donated to the Hospital. Donated assets are recorded at their estimated fair value at the date of donation.

The Hospital provides for depreciation of its plant and equipment using the straight-line method over useful lives as follows:

Land Improvements	10 - 20 Years
Buildings	20 - 40 Years
Equipment	3 - 20 Years

Self - Insured Medical, Professional and General Liability and Workers' Compensation Insurance

The Hospital records medical claims expense based upon actual employee claims reported, combined with an estimate of claims incurred but not reported based upon past experience. Claims expense is reduced by amounts recoverable through stop-loss insurance purchased by the Hospital. The Hospital is also self-insured for workers' compensation claims and in 2005 became self insured for general and professional liability. Estimates recorded for these self insured liabilities incorporate the Hospital's past experience, as well as other considerations including the nature of claims, industry data, relevant trends and/or the use of actuarial information.

Temporarily and Permanently Restricted Net Assets

Temporarily restricted net assets are those whose use by the Hospital has been limited by donors to a specific time period or purpose. Permanently restricted net assets have been restricted by donors to be maintained by the Hospital in perpetuity.

CHILDREN'S HOSPITAL

Notes to Consolidated Financial Statements

Note 2. Assets Whose Use is Limited or Restricted

Assets whose use is limited or restricted at December 31, 2009 and 2008, consist of investments as follows (in thousands):

	2009	2008
Cash and Cash Equivalents	\$ 14,886	\$ 11,212
U.S. Government Securities, Individually Owned	44,644	97,660
Corporate Bonds, Individually Owned	47,563	89,762
Corporate Bonds, Mutual Funds	3,703	6,122
Other Fixed Income Securities, Mutual Funds	116,881	4,332
Other Fixed Income, Core Bond	19,712	-
Marketable Equity Securities, Individually Owned	37,489	65,671
Marketable Equity Securities, Mutual Funds	261,349	222,194
Hedge Funds	60,188	-
Options and Futures Purchased	7	-
Options and Futures Sold	(43)	(601)
Other	68	107
Total	\$ 606,447	\$ 496,459

Investment income (loss) at December 31, 2009 and 2008, comprises the following (in thousands):

	2009	2008
Dividends and Interest Income	\$ (9,904)	\$ 18,768
Net Gains and Losses		
Realized (Losses) Gains on Sales of Securities	(24,134)	3,022
Unrealized Gains (Losses) on Securities	143,318	(253,411)
Net Gains (Losses)	119,184	(250,389)
Total Investment Income (Loss)	109,280	(231,621)
Investment Expense	(1,738)	(1,832)
Investment Income (Loss), Net	\$ 107,542	\$ (233,453)

The Hospital purchases and sells interest rate options to enhance the overall return on its investment portfolio. Interest rate options grant the purchaser, for a premium payment, the right to either purchase or sell to the writer a specified financial instrument under agreed-upon terms. The premium compensates the seller for bearing the risk of unfavorable interest rate changes. The Hospital's options on Eurodollar futures, U.S. Treasury bond futures and U.S. Treasury notes settle in cash and generally expire within one year of inception.

CHILDREN'S HOSPITAL

Notes to Consolidated Financial Statements

Note 2. Assets Whose Use is Limited or Restricted (Continued)

Futures contracts are sold or purchased to provide incremental value and to hedge or reduce market price risks. Interest rate futures contracts are commitments to either purchase or sell designated financial instruments at a future date for a specified price and may either be settled in cash or through delivery. Futures contracts have little credit risk due to daily cash settlement of the net change of open contracts. Futures on U.S. Treasury notes, U.S. Treasury bonds, and Eurodollar deposits are used due to their liquidity and credit risk advantages. Investments held by the Hospital in the amount of \$1,000,000 are pledged as collateral to secure the initial margins on futures contracts purchased.

With respect to the derivative instruments held at December 31, 2009 and 2008, the Hospital's exposure to credit-related losses in the event of nonperformance by counterparties is minimized because investment managers for the Hospital deal almost exclusively in exchange-traded futures and options. These securities are extremely liquid, are subject to rigorous exchange and government regulation, involve limited counterparty risk, have no hidden embedded risks, and have daily available public prices.

All derivative instruments are subject to market risk, which is the risk that future changes in market conditions may make an instrument less valuable or more onerous. Exposure to market risk is managed in accordance with risk limits set by the finance committee of the Board of Trustees and by monitoring performance by investment managers in accordance with specified investment guidelines. The contract amount associated with derivative instruments as of December 31, 2009 and 2008, is not considered material.

Note 3. Medicaid Program Reimbursement

The Hospital participates in the Medicaid program as a provider of medical services to program beneficiaries. Approximately 69% of the Hospital's gross patient service revenues were derived from program beneficiaries for both years ended December 31, 2009 and 2008, respectively. Inpatient services rendered to Medicaid patients are paid based on a prospective per diem system. A change in the reimbursement methodology for inpatient services is effective since September 1, 2009, and according to this new methodology, inpatient services are settled based on cost and subject to certain limitations.

Outpatient services rendered to Medicaid patients are reimbursed under a cost reimbursement methodology subject to certain limitations.

The Hospital is reimbursed for outpatient services at a tentative rate with final settlement determined after submission of annual cost reports by the Hospital and audits thereof performed by the Medicaid fiscal intermediary.

CHILDREN'S HOSPITAL

Notes to Consolidated Financial Statements

Note 3. Medicaid Program Reimbursement (Continued)

Since July 1, 1988, the Hospital has qualified as a disproportionate share provider in accordance with the State of Louisiana's Medicaid regulations and, as such, is entitled to additional payments. The Medicaid disproportionate share regulations are established by the Louisiana Department of Health and Hospitals and are subject to review and approval by the Center for Medicine and Medicaid Services. The Hospital has included \$673,000 and \$900,000 for Medicaid disproportionate share revenues in net patient service revenues for the years ended December 31, 2009 and December 31, 2008, respectively.

The Medicaid cost reports for the years 2004 through 2009 have not been finally audited by the Medicaid fiscal intermediary. Management regularly evaluates the adequacy of the recorded settlements and does not anticipate significant adverse adjustments to the recorded settlements for these cost report years. Any changes in the estimated settlements are reported as adjustments to net patient service revenues in the year the final settlements are determined. No such significant changes in estimates were recorded in 2009 and 2008.

In 2009, House Bill No. 879 (HB 879) was approved and became effective upon the signature of the Governor of Louisiana. HB 879 directed the Department of Health and Hospitals, Bureau of Health Services Financing to issue supplemental payments to hospitals that demonstrated substantial financial and operational challenges in the aftermath of hurricanes Katrina, Rita, Gustav and Ike. One of the provisions of HB 879 made additional Medicaid funding available to hospitals identified in the July 17, 2008 United States Government Accountability Office (GAO) report that have demonstrated substantial financial and operational challenges in the aftermath of Hurricane Katrina. The Hospital is one of five hospitals identified in the GAO report.

As a result of the above, the Hospital is eligible to receive supplemental payments for Medicaid services rendered. During the year ended December 31, 2009, the Hospital recognized and received as income approximately \$1,074,000 of these supplemental payments. It is expected that, during the year ended December 31, 2010, the Hospital will recognize and receive approximately \$113,000 of additional funding. This income is recorded within Net Patient Service Revenue.

CHILDREN'S HOSPITAL

Notes to Consolidated Financial Statements

Note 4. Concentration of Credit Risk

The Hospital grants credit without collateral to its patients, most of whom are local residents and are insured under third-party payor agreements. The mix of net receivables from patients and third-party payors at December 31, 2009 and 2008, was as follows:

	2009	2008
Medicaid	51 %	36 %
Managed Care	45	59
Fee-for-Service	1	1
Self-Pay and Other	3	4
Total	100 %	100 %

Note 5. Construction in Progress

In 2007, the Hospital began the PICU/CICU expansion project and has spent \$11,400,000 through the end of 2009 on this expansion. This project was substantially completed at the end of 2009, and the related expenses were transferred out of construction in progress and into fixed assets.

Note 6. Retirement Plans

The Hospital sponsors a defined contribution savings plan, which covers substantially all employees who meet age and length of service requirements. The plan allows for participating employees to make contributions ranging up to 7% of their before-tax annual compensation and provides for retirement and death benefits. The Hospital makes matching contributions equal to 50 cents per dollar for the participating employee's annual contribution up to 7% of the before-tax employee contribution. In addition, the Hospital makes a core contribution equal to 5% of the participant's annual compensation. Employees of CHMPC participate in the plan but are not eligible to receive the core contributions made by the Hospital. However, the match for the CHMPC employees is dollar for dollar for 5% of the participating employee's annual compensation. In addition, the Hospital elected to make an additional 3% discretionary contribution in 2009 and 2008. Contributions by the Hospital to this plan during the years ended December 31, 2009 and 2008, were approximately \$8,326,000 and \$7,618,000, respectively.

To comply with recent tax law changes, effective January 1, 2002, an employee becomes 100% vested in matching contributions after three full years of continuous service. Non-matching contributions and matching contributions made prior to January 1, 2002, will continue to vest after five full years of service.

CHILDREN'S HOSPITAL

Notes to Consolidated Financial Statements

Note 6. Retirement Plans (Continued)

The Hospital also sponsors an Executive Benefit Plan benefiting members of senior management. This plan includes a flexible benefit allowance account and an executive employment retention plan. These plans define specific vesting dates and provide the executive with tax deferral opportunities. Total Hospital expenses related to the Executive Benefit Plan during the years ended December 31, 2009 and 2008, were approximately \$894,000 and \$986,000, respectively. In addition, in 2002, the Hospital established a 457(b) investment account that can be utilized by senior management. As of December 31, 2009 and 2008, the Hospital's total liability for these plans is \$1,132,000 and \$677,000, respectively, and is included in accrued compensation on the consolidated balance sheets. Related assets of \$1,132,000 and \$667,000, at December 31, 2009 and 2008, respectively, are recorded to partially settle these plan liabilities.

Note 7. Insurance Programs

Prior to December 31, 2004, the Hospital was insured for professional liability malpractice claims on a claims-made basis up to \$100,000 by an insurance carrier. In 2004 the Hospital started to participate in the State of Louisiana Patients' Compensation Fund for professional liability claims in excess of \$100,000, and became self-insured for professional liability claims.

As a participant in the State of Louisiana Patient's Compensation Fund, the Hospital received malpractice coverage on a claims-made basis for claims up to \$500,000, the maximum statutory exposure that currently exists under Louisiana law, plus interest and future medical costs. All claims occurring prior to December 30, 2004, will be retained by the insurance company.

The Hospital is self-insured for workers' compensation claims up to \$500,000 in effect for fiscal periods beginning January 1, 2005 through January 1, 2010. The loss limit for workers' compensation claims was \$300,000 for fiscal periods starting January 1, 2000 through January 1, 2002, and \$350,000 for fiscal periods starting January 1, 2003 through January 1, 2004. In addition, the Hospital obtained excess workers' compensation on a claims-made basis up to \$1,000,000 through an insurance carrier in 2009 and 2008.

Prior to December 31, 2004, the Hospital was insured for general liability claims on a claims-made basis up to \$1,000,000 per incident, \$3,000,000 in the aggregate, by an insurance carrier. Effective December 31, 2004, the Hospital became self-insured for general liability claims. All claims that occurred as of December 30, 2004, will be retained by the insurance company.

CHILDREN'S HOSPITAL

Notes to Consolidated Financial Statements

Note 7. Insurance Programs (Continued)

The Hospital has purchased additional umbrella coverage on a claims-made basis of \$10,000,000 from an insurance carrier in 2009 and 2008. Hospital management believes all asserted claims are covered and will be settled within the limits of the Hospital's coverage. The recorded liability, based upon an actuarial study, totaled \$2,772,000 and \$2,071,000 at December 31, 2009 and 2008, respectively, for known claims and possible losses attributable to any workers' compensation, general, or professional liability incidents that may have occurred but that have not been identified under the Hospital's incident reporting system. This amount is recorded in accounts payable on the consolidated balance sheets.

Note 8. Community Support

The Hospital supports and participates in numerous activities and programs that benefit the community. These activities are sponsored with the knowledge that they will not be self-supporting or financially viable.

CHAP is designed to assist families with income too high to qualify for Medicaid, but whose lack of resources limit their access to quality health care. Through CHAP, the Hospital provides health care services without charge to patients whose family income is between 200% (Medicaid Limit) and 350% of the Federal Poverty Income Guidelines. In addition to CHAP, the CHMPC increases the accessibility of health care to the indigent and *underinsured* through its Kids First pediatric primary care physician practices.

The Hospital continues to focus significant efforts on supporting the advancement of medical knowledge through research. The Children's Hospital Research for Children, opened since 1997, has completed its thirteenth year of operation in 2009. Additionally, the Hospital supports the following programs: Mobile Dental Program, Children At Risk Evaluation ("CARE") Center, Inpatient Behavioral Health Program, Limited Intervention Program, the Parenting Center, Ventilator Assisted Care Program, Safe Kids Coalition, Greater New Orleans Immunization Network, Ambulatory Clinical and Nutritional Support Services, and the Miracle League.

CHILDREN'S HOSPITAL

Notes to Consolidated Financial Statements

Note 8. Community Support (Continued)

The revenues and expenses associated with these programs for the years ended December 31, 2009 and 2008, are detail ed as follows (in thousands):

2009							
	Research Institute	CHAP	Mobile Dental	CARE Center	Behavioral Health	Other	Total
Patient Revenues	\$ -	\$ 15,887	\$ 1,828	\$ 863	\$ 15,477	\$ 9,466	\$ 43,519
Revenue Deductions	-	(15,306)	(1,534)	(883)	(11,632)	(6,679)	(35,834)
Other Revenues	2,073	(2)	252	229	282	1,949	4,783
Total Revenues	2,073	579	544	409	4,127	4,736	12,468
Total Expenses	(8,303)	(4,586)	(1,512)	(1,168)	(4,691)	(5,145)	(25,405)
Community Support, Net	\$ (6,230)	\$ (4,007)	\$ (968)	\$ (759)	\$ (564)	\$ (409)	\$ (12,937)

2008							
	Research Institute	CHAP	Mobile Dental	CARE Center	Behavioral Health	Other	Total
Patient Revenues	\$ -	\$ 16,496	\$ 1,854	\$ 1,168	\$ 9,858	\$ 5,538	\$ 34,914
Revenue Deductions	-	(15,976)	(1,570)	(917)	(7,925)	(3,855)	(30,243)
Other Revenues	2,340	1,802	455	197	281	1,698	6,773
Total Revenues	2,340	2,322	739	448	2,214	3,381	11,444
Total Expenses	(8,348)	(5,451)	(1,487)	(1,273)	(3,328)	(4,352)	(24,239)
Community Support, Net	\$ (6,008)	\$ (3,129)	\$ (748)	\$ (825)	\$ (1,114)	\$ (971)	\$ (12,795)

CHILDREN'S HOSPITAL

Notes to Consolidated Financial Statements

Note 8. Community Support (Continued)

In 2009 and 2008, expenses of the community support programs include direct expenses and an allocation of indirect expenses as follows (in thousands):

	2009	2008
Direct Expenses	\$ 16,683	\$ 14,952
Indirect Expenses	8,722	9,287
Total Expenses	\$ 25,405	\$ 24,239

Indirect expenses represent estimates of patient care cost and allocated overhead using Medicare cost reporting methodologies.

In addition to the above community support activities, the Hospital provides additional benefits to Medicaid patients in the form of uncompensated patient care costs. The Hospital also emphasizes the importance of higher education and funds the teaching of students and health professionals through a comprehensive graduate medical education program.

Note 9. Assets Held in Trust

The Hospital has been named the income beneficiary of a separate trust. Because the assets of the trust are not controlled by the Hospital and the Hospital does not have an irrevocable right to receive the income earned on the trust's assets, they are not included in the Hospital's financial statements. The assets had a market value of approximately \$3,892,000 and \$3,653,000, at December 31, 2009 and 2008, respectively. Distributions of income are made at the discretion of the trustee. In 2009 and 2008, the Hospital recorded contribution income of approximately \$142,000 and \$161,000, respectively, received from the trust.

Note 10. Functional Expenses

The Hospital provides inpatient and outpatient health care services to patients in the Gulf South region. Expenses related to providing these services for the years ended December 31, 2009 and 2008, are as follows (in thousands):

	2009	2008
Health Care Services	\$ 180,258	\$ 173,903
Administrative and Fiscal	33,715	27,036
Total	\$ 213,973	\$ 200,939

CHILDREN'S HOSPITAL

Notes to Consolidated Financial Statements

Note 11. Temporarily Restricted Net Assets

Temporarily restricted net assets at December 31, 2009 and 2008, are available as follows (in thousands)

	2009	2008
Capital Additions	\$ 1,887	\$ 2,166
Research, Education, and Other	2,173	2,422
Total	\$ 4,060	\$ 4,588

Note 12. Operating Leases

The Hospital has a number of operating leases of clinic sites. For these leases, the Hospital has, as of December 31, 2009, contractual agreements requiring the following annual rental payments (in thousands):

Fiscal Year Ending December 31, 2010	Amount
2010	\$ 877
2011	708
2012	615
2013	455
2014	360
2015-2017	994
Total	\$ 4,009

Rental expenses for these leases consisted of \$1,463,000 and \$1,188,000, for the years ended December 31, 2009 and 2008, respectively.

Note 13. Fair Value Measurements

The carrying values of the Hospital's financial instruments, including current assets and current liabilities, approximate fair value.

CHILDREN'S HOSPITAL

Notes to Consolidated Financial Statements

Note 13. Fair Value Measurements (Continued)

In 2008, the Hospital adopted the provisions of the Financial Accounting Standards Board (FASB) Accounting Standards Codification (ASC) Fair Value Measurements Topic. Under the Fair Value Measurements Topic of the FASB ASC, fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

The Fair Value Measurements Topic of the FASB ASC establishes a fair value hierarchy for inputs used in measuring fair market value that maximizes the use of observable inputs and minimizes the use of unobservable inputs by requiring that the most observable inputs be used when available. Observable inputs are those that market participants would use in pricing the asset or liability based on the best information available in the circumstances. The fair value hierarchy is categorized into three levels based on the inputs as follows:

Level 1 - Valuations based on unadjusted quoted prices in active markets for identical assets or liabilities as of the reporting date. Since valuations are based on quoted prices that are readily and regularly available in an active market, valuation of these securities does not entail a significant degree of judgment.

Level 2 - Valuations based on quoted prices in markets that are not active or for which all significant inputs are observable, either directly or indirectly, as of the reporting date.

Level 3 - Valuations based on inputs that are unobservable and include situations where there is little, if any, market activity for the investment. The inputs into the determination of fair value require significant management judgment or estimation.

In some instances, the inputs used to measure fair value may fall into different levels of the fair value hierarchy. In such instances, an investment's level within the fair value hierarchy is based on the lowest level of input that is significant to the fair value measurement.

CHILDREN'S HOSPITAL

Notes to Consolidated Financial Statements

Note 13. Fair Value Measurements (Continued)

The valuation of the Hospital's assets and liabilities measured at fair value on a recurring basis at December 31, 2009 is as follows (in thousands):

	Level 1	Level 2	Level 3	Net Balance
Assets whose Use is Limited or Restricted	\$ 377,351	\$ 71,676	\$ 157,420	\$ 606,447
Total	\$ 377,351	\$ 71,676	\$ 157,420	\$ 606,447

The changes in investments measured at fair value for which the Hospital has used Level 3 inputs to determine fair value are as follows (in thousands):

Level 3 Beginning Balance January 1, 2009	Realized and Unrealized Gains (Losses)	Purchases, Sales and Settlements	Net Transfers In and/or (Out) of Level 3	Level 3 Ending Balance December 31, 2009
\$ -	\$ 635	\$ 156,785	\$ -	\$ 157,420

The valuation of the Hospital's assets and liabilities measured at fair value on a recurring basis at December 31, 2008 is as follows (in thousands):

	Level 1	Level 2	Level 3	Net Balance
Assets whose Use is Limited or Restricted	\$ 496,459	\$ -	\$ -	\$ 496,459
Total	\$ 496,459	\$ -	\$ -	\$ 496,459

Note 14. Related Party Transactions

Louisiana Children's Medical Center (LCMC) provided a Health Care System Agreement dated July 13, 2009. This agreement provides, amongst other items, that LCMC will act as a System Parent with LCMC being the sole member of Touro Infirmary and of Children's Hospital. This agreement also provides that Children's Hospital and LCMC covenant and agree that over the period beginning at the effective date of the agreement, and ending on the earlier of the five-year anniversary of the effective date or the date upon which the commitment funds have been expended, a minimum of \$100 million shall be expended or legally obligated through a binding contract for the acquisition of capital items to benefit Touro Infirmary and its subsidiaries (Touro Group).

CHILDREN'S HOSPITAL

Notes to Consolidated Financial Statements

Note 14. Related Party Transactions (Continued)

The commitment funds to be transferred will be determined by LCMC and will be conditioned on the determined need for such funds in excess of annual cash flow activities, as defined, of the Touro Group. Due to this conditional pledge, Children's Hospital will not recognize an expense until the funds are remitted to Touro. During the year ended December 31, 2009, Children's Hospital provided funding under this agreement in the amount of \$3.1 million. This amount is included within non-operating income (loss) on the consolidated statement of operations.

In 2009, Children's Hospital was assessed a management fee by LCMC for management services provided directly to Children's Hospital. The amount of these services was \$810,709, and is included within professional fees on the consolidated statement of operations. Touro was also assessed a management fee in the amount of approximately \$206,000. Children's initially incurred these costs on behalf of LCMC and is owed this amount by LCMC, who in turn has a receivable from Touro for the same amount.

During 2009, Children's Hospital paid \$1.4 million to the Jewish Federation of Greater New Orleans (Federation), on behalf of the Touro Group. This payment was made in relation to a commitment of the Touro Group to the Federation, and is reflected on the consolidated statement of operations within non-operating income (loss).

Children's receives certain services from Touro. These services consist of nurse certification training, benefit events, medical staff facility privileges, and office space rental for a primary care clinic. The total payments made by Children's for these services was approximately \$113,000 for the year ended December 31, 2009, and is included within operating expenses on the consolidated statement of operations.

Children's Hospital has assumed the role of the guarantor of defined swap agreements that have been entered into by Touro. As such, Children's unconditionally guarantees the prompt payment of all liabilities associated with those swap agreements. This guarantee shall remain in force until such time as Touro Infirmary has fully satisfied its obligations under the swap agreements.

CHILDREN'S HOSPITAL

Notes to Consolidated Financial Statements

Note 15. Accounting for Uncertainty in Taxes

For the year ended December 31, 2009, Children's adopted the provisions of the Accounting for Uncertainty in Income Taxes Topic of the FASB ASC. Children's recognizes a threshold and measurement process for financial statement recognition of uncertain tax positions taken or expected to be taken in a tax return. The interpretation also provides guidance on recognition, derecognition, classification, interest and penalties, accounting in interim periods, disclosure and transition. Children's tax filings are subject to audit by various taxing authorities. Children's open audit periods are 2006 through 2009. There are currently no returns under examination. Management evaluated Children's tax positions and considered that Children's had taken no uncertain tax positions that require adjustments to the financial statements to comply with the provisions of this guidance.

Note 16. Subsequent Events

Management has evaluated subsequent events through the date that the financial statements were available to be issued, April 26, 2010, and determined that no events occurred that require disclosure. No subsequent events occurring after this date have been evaluated for inclusion in these financial statements.

CHILDREN'S HOSPITAL

Single Audit Report

For the Year Ended December 31, 2009

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**Independent Auditor's Report on Internal Control Over Financial
Reporting and on Compliance and Other Matters Based
on an Audit of Financial Statements Performed in
Accordance with Government Auditing Standards**

Children's Hospital
New Orleans, Louisiana

We have audited the financial statements of Children's Hospital (the Hospital), as of and for the year ended December 31, 2009, and have issued our report thereon dated April 26, 2010. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Hospital's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Hospital's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Hospital's internal control over financial reporting.

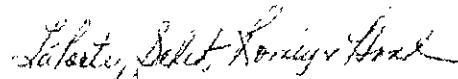
A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Hospital's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information of the Audit Committee, management, the Legislative Auditor of the State, federal awarding agencies, and pass-through entities and is not intended to be, and should not be, used by anyone other than these specified parties. Under Louisiana Revised Statute 24:513, this report is distributed by the Legislative Auditor as a public document.

A handwritten signature in black ink, appearing to read "Robert J. Koenig".

A Professional Accounting Corporation

April 26, 2010



**Report on Compliance with Requirements Applicable
to Each Major Program and Internal Control
Over Compliance in Accordance with OMB Circular A-133**

Children's Hospital
New Orleans, Louisiana

Compliance

We have audited the compliance of Children's Hospital (the Hospital) with the types of compliance requirements described in the U. S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended December 31, 2009. The Hospital's major federal programs are identified in the summary of auditor's results section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of the Hospital's management. Our responsibility is to express an opinion on the Hospital's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Hospital's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of the Hospital's compliance with those requirements.

In our opinion, the Hospital complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended December 31, 2009.

Internal Control Over Compliance

The management of the Hospital is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs.

In planning and performing our audit, we considered the Hospital's internal control over compliance with the requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Hospital's internal control over compliance.

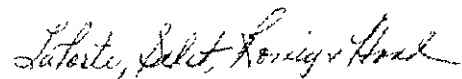
A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

Schedule of Expenditures of Federal Awards

We have audited the basic financial statements of the Hospital, as of and for the year ended December 31, 2009, and have issued our report thereon dated April 26, 2010. Our audit was performed for the purpose of forming an opinion on the basic financial statements taken as a whole. The accompanying schedule of expenditures of federal awards is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in our audit of the basic financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the basic financial statements taken as a whole.

This report is intended solely for the information and use of the Audit Committee, management, the Legislative Auditor of the State, federal awarding agencies, and pass-through entities and is not intended to be, and should not be, used by anyone other than these specified parties. Under Louisiana Revised Statute 24:513, this report is distributed by the Legislative Auditor as a public document.



A Professional Accounting Corporation

April 26, 2010

CHILDREN'S HOSPITAL
Schedule of Expenditures of Federal Awards
For the Year Ended December 31, 2009

Federal Grantor/Pass-Through Grantor Program Title	Federal CFDA Number	Pass-Through Entity No.	Federal Revenue/ Expenditures Recognized
Research and Development Cluster			
Department of Health and Human Services - National			
Institutes of Health:			
G-Protein Signaling Cryptococcus Neoforms Mechanisms of Antibody-Medicated Toxin Neutralization	93.855		\$ 44,343
Atypical G-Protein Signaling in Cryptococcus Neoformans	93.855		163,442
Nanopore Study of Single Antibody/Antigen Interactions	93.855		264,281
Development of a Vaccine Against Helicobacter Pylori to Prevent Gastric Cancer	93.879		43,791
Microbial Correlates of Bacterial Vaginosis Treatment Failure and Recurrence in H	93.393		21,303
ARRA - Atypical G Protein Signaling in Cryptococcus Neoformans	93.855		366,498
ARRA - Transcription Factors in Neuroendocrine Differentiation	93.701		92,074
Antioxidant Protection	93.701		39,624
	93.847		305,742
Passed Through Programs From:			
Tulane University- Research Commercialization and Education Enhancement Program	93.RD	TUL-HSC-108-08/09	55,800
University of Pittsburg - Mycology Research Unit in Vivo Induced Fungal Antigens	93.855	P01A1061537	42,170
Louisiana State University Mechanical College Mechanisms for the Metabolic Syndrome in Prepubertal African American & Caucasian Youth	93.865	R01HD049046	99,107
Fox Chase Cancer Center-Adolescent Diet, Hormone & Breast Cancer Susceptibility	93.399	R01CA104670	8,991
University of New Orleans Highly Sensitive & Selective Chemical & Biological Sensor Chips	12.910	HR0011-07-10032	33,299
Louisiana State University Mechanical College Minority-Based Community Clinical Oncology Program	93.399	CA063845	72,941
University of Pittsburg - Novel Bacterial Pathogens in Pelvic Inflammatory Disease	93.855	1R01A1073940-01A1	56,035
Washington University - Tilton CTC Oral Baclofen Study	47.074	HHSN267200603421C	77,621
Total Research and Development Cluster			<u>1,787,062</u>

See accompanying notes to schedule of expenditures of federal awards.

CHILDREN'S HOSPITAL
Schedule of Expenditures of Federal Awards (Continued)
For the Year Ended December 31, 2009

Federal Grantor/Pass-Through Grantor Program Title	Federal CFDA Number	Pass-Through Entity No.	Federal Revenue/ Expenditures Recognized
Department of Health and Human Services:			
Health Resources and Services Administration-			
Ryan White Title IV Program	93.153		1,984,499
Children's Hospitals Graduate Medical Education			
Payment Program	93.255		4,232,771
Total Other DHHS Programs			<u>6,217,270</u>
Passed Through Programs From:			
City of New Orleans Ryan White Case Management	93.914	K09-614	220,527
City of New Orleans Ryan White Mental Health	93.914	K09-614	76,454
City of New Orleans Ryan White Medical Transportation	93.914	K09-614	76,614
City of New Orleans Ryan White Non Medical			
Case Management	93.914	K09-1031	35,001
City of New Orleans Ryan White Medical Case			
Management	93.914	K08-1025	47,408
State of Louisiana:			
Law Enforcement and Administration of Criminal			
Justice-Child Advocacy Program	16.582	C09-9-006	50,324
Office of Community Services	93.670	555302 370 100896	23,799
Louisiana Office of Public Health:			
Diabetes Contract	93.994	B04MC07804	123,573
Primary Care Access & Stabilization	93.776	1M0CMS030175/01	2,000,944
Department of Education-Special Education	84.027A	H037A050033	117,098
Total Other Pass-Through Programs			<u>2,771,742</u>
Total Expenditures of Federal Awards			<u><u>\$ 10,776,074</u></u>

See accompanying notes to schedule of expenditures of federal awards.

CHILDREN'S HOSPITAL

Notes to Schedule of Expenditures of Federal Awards For the Year Ended December 31, 2009

Note 1. Basis of Presentation

The accompanying schedule of expenditures of federal awards includes the federal grant activity of Children's Hospital and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*.

Note 2. Subrecipients

Of the federal expenditures presented in the schedule, Children's Hospital provided federal awards to subrecipients as follows:

Program Title	Federal CFDA Number	Amount Provided to Subrecipients
Ryan White Title IV Program	93.153	\$ 840,033
B-cells in Pups of Mild & Severe STZ Diabetic Mothers; Antioxidant Protection	93.847	13,881
Microbial Correlates of Bacterial Vaginosis Treatment Failure and Recurrence in H	93.855	134,835

CHILDREN'S HOSPITAL

**Schedule of Findings and Questioned Costs
For the Year Ended December 31, 2009**

Part I - Summary of Auditor's Results

Financial Statement Section

Type of auditor's report issued: Unqualified

Internal control over financial reporting:

Material weakness(es) identified? No

Significant Deficiency(ies) identified that are not considered to be material weakness? None Reported

Noncompliance material to financial statements noted? No

Federal Awards Section

Internal control over major programs:

Material weakness(es) identified? No

Significant deficiency(ies) identified that are not considered to be material weaknesses? None Reported

Type of auditor's report issued on compliance for major programs: Unqualified

Any audit findings disclosed that are required to be reported in accordance With Circular A-133 (section .510(a))? No

Identification of major programs:

Title

CFDA Number

Children's Hospitals Graduate Medical Education
Payment Program

93.255

Dollar threshold used to determine Type A programs: \$300,000

Auditee qualified as low-risk auditee? Yes

CHILDREN'S HOSPITAL

Schedule of Findings and Questioned Costs (Continued)
For the Year Ended December 31, 2009

Part II - Schedule of Financial Statement Findings Section

No findings were noted.

Part III - Federal Awards Findings and Questioned Costs Section

No findings were noted.

CHILDREN'S HOSPITAL

**Management's Summary Schedule of Prior Audit Findings
For the Year Ended December 31, 2009**

None.